# ECONOMIC REPORT

## 3.0 DEVELOPMENTS IN THE ECONOMY

### 3.1 Monetary and Credit Developments

Monetary management was driven largely by the liquidity condition and the operation of the new framework for monetary policy implementation, which commenced in December 2006. Various policy actions were taken in the review period to ensure that targets for monetary aggregates under the Policy Support Instrument (PSI) were met. The two-way quote trading between the CBN and Money Market Dealers (MMDs) and the pilot run for trading among MMDs commenced in June 2007.

Following the relative macroeconomic stability evidenced by the downward trend in inflation and the viability of the external sector, the Monetary Policy Rate (MPR) was reviewed downwards by 200 basis points, from 10.0 to 8.0 per cent in June. Similarly, the interest rate corridor was reduced from 600 to 500 basis points. Consequently, the rates of the CBN deposit and lending facilities stood at 5.5 and 10.5 per cent, down from 7.0 and 13.0 per cent.

Available data indicated that broad money ($M_2$) increased by 11.01 per cent to N4,079.4 billion in June 2007, compared with the 29.1 per cent in the corresponding period of 2006, respectively. On an annualized basis, this represented a growth of 22.02 per cent, compared with the target of 19.0 per cent for fiscal 2007. Narrow money supply ($M_1$) rose modestly by 0.63 per cent to N1, 947.2 billion, compared with 20.4 per cent growth in the corresponding period of 2006. The growth in money stock reflected the increase in foreign and other assets (net) of the banking system.

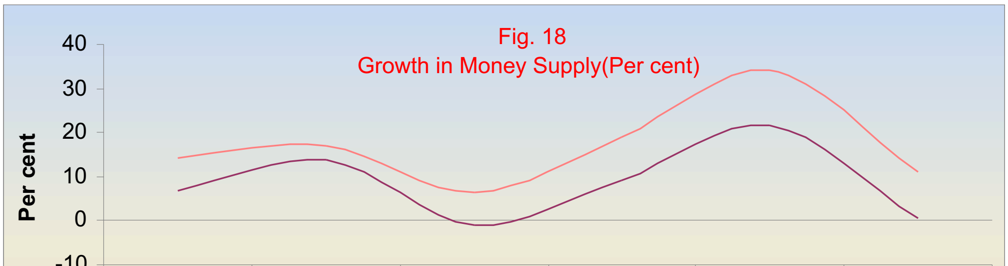


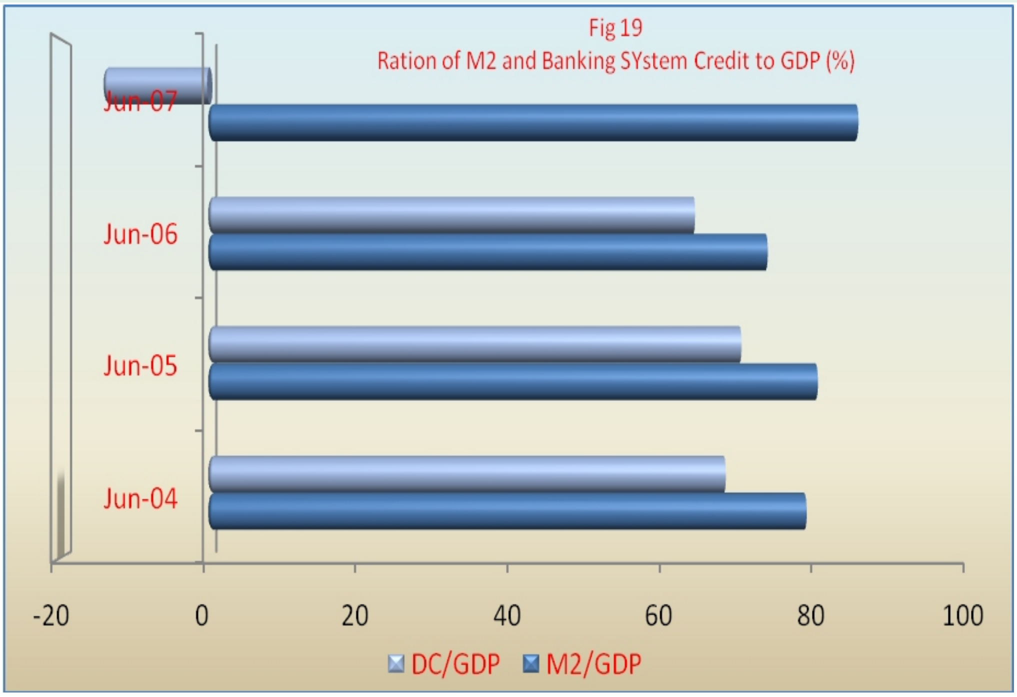
Fig. 18
Growth in Money Supply(Per cent)

| | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 |
|---|---|---|---|---|---|---|
| M1 | 6.8 | 13.8 | -0.9 | 9.3 | 21.5 | 0.63 |
| M2 | 14.2 | 16.9 | 6.5 | 18.9 | 34.1 | 11.01 |

#### 3.1.1 Drivers of Growth in Monetary Aggregates

##### 3.1.1.1 Net Foreign Assets (NFA)

The rise in the components of monetary liabilities was attributable largely to the increase in the Net Foreign Assets of the banking system. The NFA increased by 23.2 per cent over its level at end-December 2006, owing to the favourable crude oil prices in the international oil market. NFA, as a percentage of M2 stood at 187.8 per cent compared with 194.9 and 164.7 per cent at end-December 2006 and the corresponding period of 2006, respectively.




### 3.1.1.2 Net Domestic Asset

The net domestic assets (NDA) of the banking system, at negative N3, 581.1 billion, had a moderating effect on the growth of M2 as it showed a decline of 40.7 and 43.0 per cent below the levels at end-December 2006 and the corresponding end-June 2006. The decline in NDA was entirely due to the decline in net domestic credit, which more than offset the increase in other assets (net) of the banking system.

### 3.1.1.3 Net Domestic Credit (NDC)

Credit to the domestic economy fell by 187.2 per cent at end-June 2007 relative to the level at end-December 2006. The development reflected wholly the decline in net credit to the government, following the increase in Federal Government deposits with the banking system.

### 3.1.1.4 Credit to the Government (Cg)

Net credit to the Government fell by 126.0 per cent, compared with 17.89 per cent at end-June 2006, reflecting the significant increase in Federal Government deposits with the banking system, particularly with the CBN. Thus, the Federal Government was a net creditor to the banking system during the period.

### 3.1.1.5 Credit to the Private Sector (Cp)

Credit to the private sector, including the State and Local Governments, non-financial public enterprises and the core private sector, rose significantly by 34.4 per cent over the level at end-December 2006. The effect of this development on the NDC was more than offset by the substantial decline in credit to the Federal Government (net). The core private sector was the major beneficiary of the increase in credit to the private sector.

Analysis of the banking system flow of credit to the private sector showed that at end- June, 2007, oil and gas, communications and other sectors, attracted 39.4, 25.0 and 9.8 per cent respectively of the total credit to the private sector. The priority sectors, namely agriculture, manufacturing, mining and quarrying and exports had a share of 1.9, 12.6, 10.0 and 1.40 per cent, respectively. Relative to December 2006, credit to oil and gas, communication and unclassified sectors grew by 52.1, 33.7 and 56.1 per cent respectively, while that to agriculture, and mining and quarrying increased by 22.2 and 35.1 per cent, respectively. However, credit to the manufacturing and exports sub- sectors, declined by 4.6 and 9.7 per cent, respectively, comp ared with the levels at end- December, 2006.

Fig. 20
Share of Government and Private Sector in Banking System's Credit to the Economy

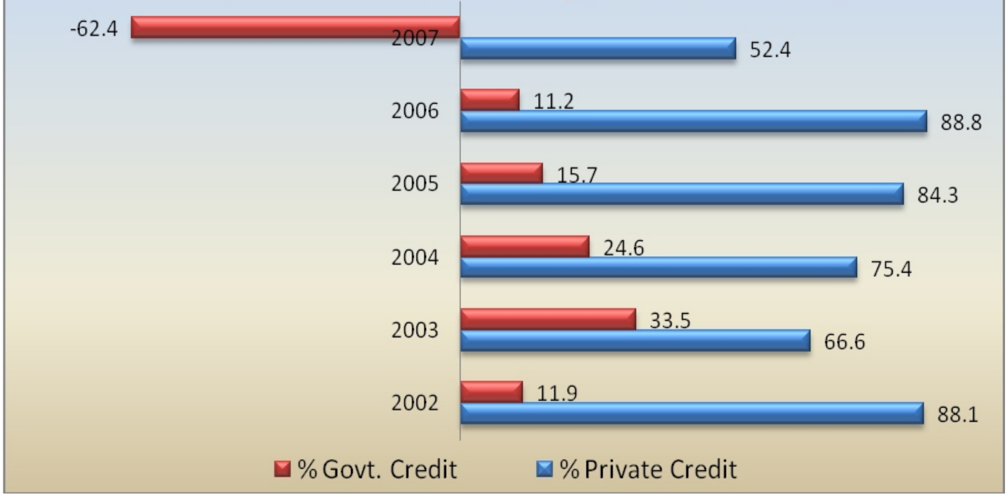
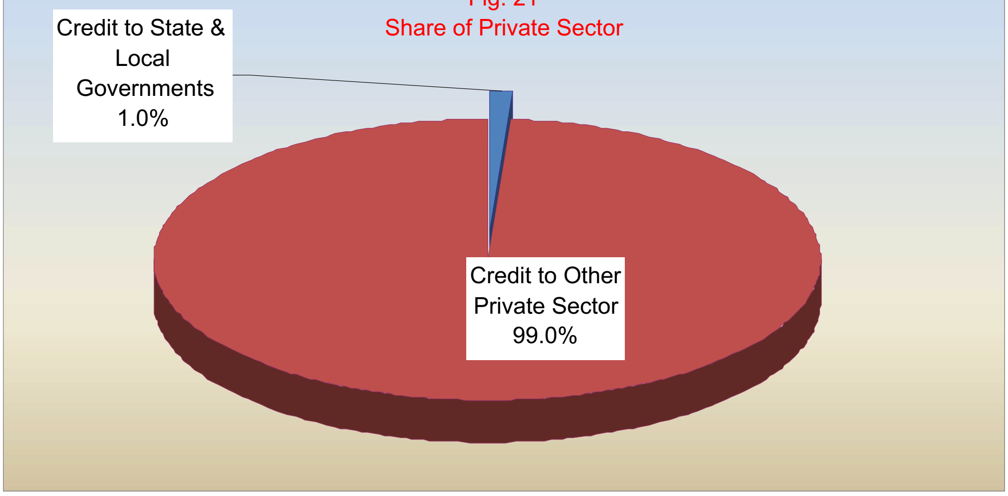



Fig. 21
Share of Private Sector




### 3.1.2 Money Market Developments

Activities in the money market in the first half of 2007 indicated improved performance. Public offers of government securities at the primary market were over-subscribed due to the short-supply of risk-free, long tenored securities with more attractive yields. Foreign investors' patronage at the primary market was also sustained indicating improved confidence in the economy.

### 3.1.2.1 Money Market Assets Outstanding

Available data indicated that the level of money market assets outstanding at end-June, 2007 stood at N2,032.2 billion, showing an increase of 24.0 and 16.93 per cent over the levels at end-December and June 2006, respectively. The development reflected largely, the increase of 42.0, 22.4 and 41.9 per cent in Commercial Papers (CPs), Bankers' Acceptances (BAs) and FGN Bonds, respectively.

### 3.1.2.2 Primary Market

The Debt Management Office (DMO) in collaboration with the CBN, issued 3- , 5- and 7-year tenored FGN Bonds worth N270.00 billion in the first half of the year, compared with N175.9 billion issued in the corresponding period of 2006. The bonds were partly for the settlement of debt owed to Federal Government contractors and pension arrears. Total subscription and allotments were N611.26 billion and N281.7 billion, respectively, compared with N335.5 billion and N174.5 billion in the first half of 2006. The significant increase in subscription was attributable to the market players' continued preference for longer tenored securities with more attractive yield. To further enhance activities in the bond market, the DMO appointed additional five (5) primary market dealers, thus bringing the total number of dealers to twenty (20), comprising the five (5) discount houses and fifteen (15) deposit money banks.

Treasury bills issued to replace maturing ones amounted to N783.31 billion, compared with N801.0 billion in the corresponding period of 2006. The development was attributable to the low volume of instruments on offer during the period. However, the sustained patronage in the primary market was due to market players' preference for risk-free assets.

Treasury bills holdings declined by 16.13 per cent from its level at end-June 2006. The decline was attributable to the repayment of matured bills. Analysis of the holdings of outstanding TBs showed that the deposit money banks and discount houses jointly increased their investments by 24.4 per cent to N647.7 billion. However, holdings by the non-bank public fell by 56.1 per cent to N68.6 billion. The CBN's holding of treasury bills outstanding amounted to N0.6 billion, compared with N40.5 billion in the corresponding period of 2006.

### 3.1.2.3 Open Market Operations (OMO)

Open Market Operations (OMO) remained the major tool for liquidity management. In line with the new framework for monetary policy implementation, the tenors at the auctions were structured to synchronise the maturities with those in the primary auctions, thus ensuring that tradable maturities were available to the market. To further enhance efficiency in the financial market, the two-way quote trading in securities commenced in June 2007.

Total subscription and sales amounted to N411.8 billion and N1,051.0 billion, respectively, compared with N1,207.0 billion and N895.6 billion in the corresponding period of 2006. The increased sale was attributable to the commencement of the two-way quote trading in government securities, the attractive yields and the dearth of the long-tenored instruments.

### 3.1.2.4 Interest Rates Developments

The Monetary Policy Rate (MPR) was reviewed downwards by 200 basis points, from 10.0 per cent to 8.0 per cent in June in line with the prevailing macroeconomic fundamentals. Similarly, the interest rate corridor was reduced from 600 to 500 basis points.

### 3.1.2.5 Money Market Rates

Volatility of rates was subdued as inter-bank rates generally fell within the standing facility's interest rate corridor, fluctuating around the MPR. The development reflected the salutary effect of the new CBN monetary policy implementation framework. The inter-bank call rate was 8.46 per cent at end-June 2007, compared with 8.16 per cent in the corresponding period of 2006. The average Open Buy-Back (OBB) rate stood at 7.75 per cent, down from 10.63 per cent in the first half of 2006.The weighted average of the Nigeria Inter-bank Offered Rate (NIBOR) for the 7- and 30-day tenors were 7.87 and 10.82 per cent, respectively, compared with 8.21 and 11.80 per cent in the first half of 2006.

**Box 1: The CBN Standing Facility**

The CBN Standing Facility is a component of the new framework for monetary policy implementation which commenced on December 11, 2006. The corridor created by the spread between the lending facility which is the upper band and the deposit facility which is the lower band of fluctuation, was designed to achieve inter-bank rate stability by influencing the overnight short-term money market interest rates. It provides the financial valves for absorbing surplus funds and injecting over night funds on a last resort basis. Furthermore, the lending and deposit facilities provide the corridor within which market players with suitable securities are expected to trade. Under the arrangement, DMBs with surplus funds deposited them at 5.5 per cent (250 basis points below the MPR), while those that were short of funds borrowed at 10.50 per cent (250 basis points above the MPR). The operation of the scheme had a salutary effect in moderating inter-bank rates in the first half of 2007.

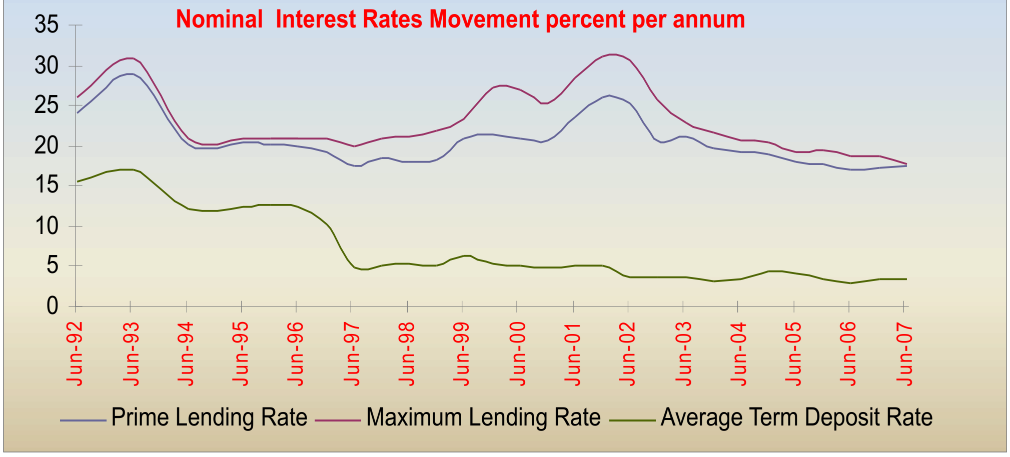
### 3.1.2.6 Deposit Rates

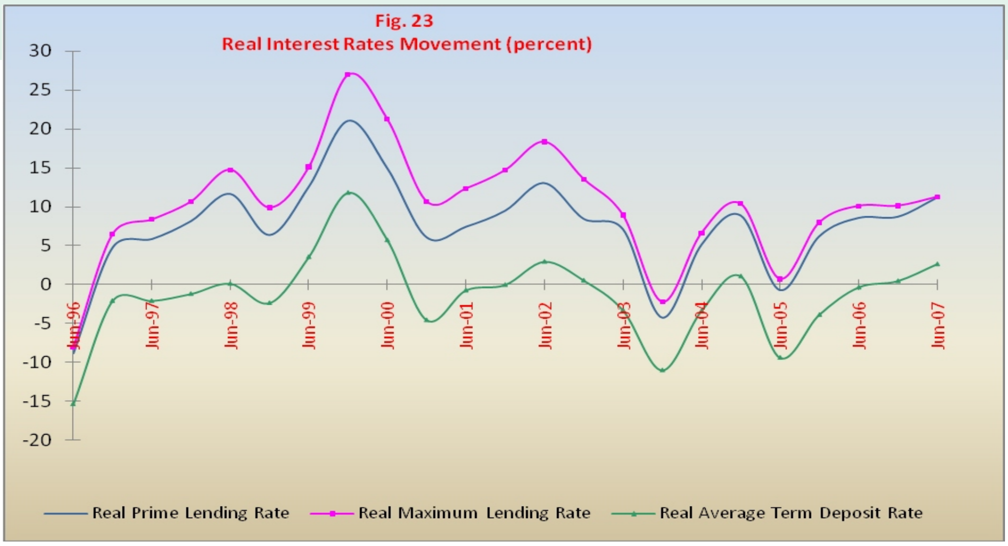
The rising trend observed in banks' deposit rates since 2006 persisted. The average savings deposit rate rose by 0.21 percentage point over the end-December 2006 level to 3.46 per cent. Other rates on deposits of various maturities also rose from a range of 5.21  10.25 per cent in December 2006 to 5.37  10.35 per cent at end-June, 2007, reflecting the increased competition in the banking system.

### 3.1.2.7 Lending Rates

The declining trend that was observed in banks' average prime lending rate was reversed in 2007. The average prime lending rate, rose from 17.15 per cent at-end December 2006 to 17.63 per cent at end-June 2007. This development can be attributed to inflation expectation. The average maximum lending rate, however, declined from 18.59 per cent at end-December 2006 to 17.68 per cent. Thus, the spread between banks' average term deposit and maximum lending rates narrowed to 8.71 percentage points at end-June 2007 from 10.31 percentage points in the corresponding period of 2006. With the year-on-year inflation rate at 6.4 per cent in June 2007, most of the term deposit rates were positive in real terms.

Fig. 22
Nominal Interest Rates Movement percent per annum






### 3.1.3 Institutional Savings

Aggregate institutional savings as at end-June 2007, amounted to N2,345.4 billion, indicating an increase of 2.6 per cent over the level in the corresponding period of 2006. The DMBs, buoyed by the deposit of N650 billion under the Pension Fund Scheme, remained the dominant savings institution, accounting for 90.0 per cent of the total institutional savings at end-June 2007, compared with 90.9 and 94.0 per cent at end-June and end-December 2006, respectively. Other institutions, including primary mortgage, life insurance funds, the Nigerian Social Insurance Trust Fund, and community/microfinance banks held the balance of 10.0 per cent. The ratio of institutional savings to GDP (2007) was 21.9 per cent compared with 19.5 per cent in the corresponding period of 2006.

### 3.1.4 Other Financial Institutions

#### 3.1.4.1 Development Finance Institutions

Five out of the six development finance institutions namely: Bank of Industry (BOI), Federal Mortgage Bank of Nigeria (FMBN), Nigerian Export Import Bank (NEXIM), Nigerian Agricultural, Co-operative and Rural Development Bank (NACRDB) and Urban Development Bank (UDB) had aggregate assets of N134.7 billion at end-June 2007. This was N55.1 billion or 62.2 per cent higher than the level in December 2006. However, two DFIs, namely the Federal Mortgage Bank and the Urban Development Bank had negative shareholders' funds as at end-June. The aggregate shareholders' funds of the DFIs increased by 2.1 per cent to N21.87 billion over the end-December 2006 level.

#### 3.1.4.2 Community / Micro Finance Banks

The total assets/ liabilities of the reporting Community Banks (CBs) increased by 1.8 per cent over the end-December 2006 level to N56.08 billion in June 2007. The paid-up share capital and shareholders' fund increased by 1.71 and 7.84 per cent to N8.44 billion and N13.74 billion, respectively. Loans and advances granted by the reporting banks increased by 0.6 per cent to N16.50 billion.

#### 3.1.4.3 Discount Houses

Total assets/liabilities of the five operating discount houses as at end-June 2007 rose by 33.6 per cent to N223.6 billion, compared with the level in the corresponding period of 2006. The total funds sourced amounted to N104.6 billion, compared with N91.9 billion at end-June 2006. The funds were sourced mainly from an increase in “other amount owed to customers” (N53.9 billion) and “claims on banks” (N41.4 billion), among others. The funds were utilized mainly in the purchase of Federal Government securities of less than 91-days maturity (N57.0 billion), and settlements of claims (N19.4 billion). Discount houses' investments in Federal Government securities of less than 91 days maturity amounted to N104.3 billion at end-June 2007, representing 46.7 per cent of their total deposit liabilities. This was 13.3 percentage points below the prescribed minimum of 60.0 per cent for fiscal 2007.

#### 3.1.4.4 Finance Companies (FCs)

The total number of licensed finance companies (FCs) stood at 113, same as end-December 2006 due to the suspension of the issuance of new licenses. Total capitalization of the FCs rose to N13.44 billion from N11.37 billion at end-December 2006. The total assets/ liabilities of the FCs increased by 6.04 per cent to N57.60 billion at end-June 2007. Loans and advances increased by 1.23 per cent to N24.14 billion in June 2007, while placements with other FCs increased by 27.98 per cent to N11.89 billion. Total borrowing, however, declined by 0.91 per cent to N34.33 billion in June 2007. Investible funds accruing to the sub-sector was N5.27 billion.

#### 3.1.4.5 Primary Mortgage Institutions (PMIs)

The total number of licensed PMIs remained at 91 as at end- December 2006. Three PMIs were, however, given approval to restructure their capital base, bringing the total number of PMIs undergoing restructuring to eight (8), while approval was given to Diamond Mortgages Limited to access the National Housing Fund (NHF) warehoused at the Federal Mortgage Bank of Nigeria (FMBN). Total capitalization increased by 0.4 per cent to N15.62 billion, while the total assets of the PMIs increased by 5.7 per cent to N120.95 billion at end-June 2007. Investible funds available to the PMIs totaled N 28.86 billion.

#### 3.1.4.6 Bureaux-de-Change (BDCs)

One hundred and ten (110) fresh applications for BDC licences were received, out of which sixteen (16) operating licences were approved and sixty-six (66) Approvals-In-Principle were granted, while twenty-eight (28) others were at various stages of processing. Consequently, the number of BDCs in the country therefore rose to 368 at end-June 2007, compared with 352 at end-December 2006.

#### 3.1.4.7 Pension Fund Administrators/Custodians

As at end-May, 2O07, 23 Pension Fund Administrators (PFAs) had been licensed by the National Pension Commission, each with a paid-up share capital of N150 million. Also four (4) Pension Funds Custodians were licensed. The sum of N650 billion was collected from 2.4 million registered employees under the scheme as at end-May 2007 out of the 18 million targeted Nigerian workers.

**Box 2: Pension Fund Reforms**

Consistent with the key elements of the Federal Government's medium term reform and development agenda, the National Economic Empowerment and Development Strategy (NEEDS), a pension reform Act was initiated in 2004 in order to address the problems associated with the old pension schemes in the country. Specifically, the reform was intended to

- reduce fiscal cost of pension administration to the government, achieve fiscal reform through measures designed to raise domestic savings and increase private investments, mobilize long-term savings to finance the real sector to sustain high and broad based GDP growth, and promote the development of an efficient capital market.

The new pension scheme requires pension funds to be privately managed by licensed Pension Fund Administrators and Custodians. The Pension Fund Custodians (PFCs) are responsible for warehousing the pension fund assets, while the PFAs are responsible for the day to day administration of the retirement savings account of the employees but are not allowed to hold the pension funds assets. The employer sends the contributions directly to the Custodians, who notify the PFA of the receipt of the contribution and the PFA subsequently credits the retirement savings account of the employee.

The PFAs open retirement savings accounts for employees, manage the pension funds as the Commission may from time to time prescribe, maintain books of accounts on all transactions relating to the pension funds under their management, provide regular information to the employees or beneficiaries and pay retirement benefits to employees in accordance with the provisions of the Pension Reform Act 2004. Pension Funds Custodians were required to have a minimum net worth of N5 billion and a total balance sheet of not below N125 billion.

The pension funds market has a projected annual growth rate of about 15 per cent and it is expected that the development of the pensions sector will help create the market for long term securities such as bonds, mortgages and asset-backed securities. It will also help in developing competencies in asset management and custodianship.

### 3.1.5 Capital Market Developments

#### 3.1.5.1 The Nigerian Stock Exchange

The performance of the Nigerian Stock Exchange improved significantly as reflected in the increased activities in both the primary and secondary segments of the market. Market capitalization of the 302 listed securities increased by 154.3 per cent to close at N8.9 trillion, compared with N3.5 trillion at end-June 2006. When compared with the end-December 2006 level of N5.12 trillion, this represented a rise of 74.5 per cent.

#### 3.1.5.2 New Issues Market

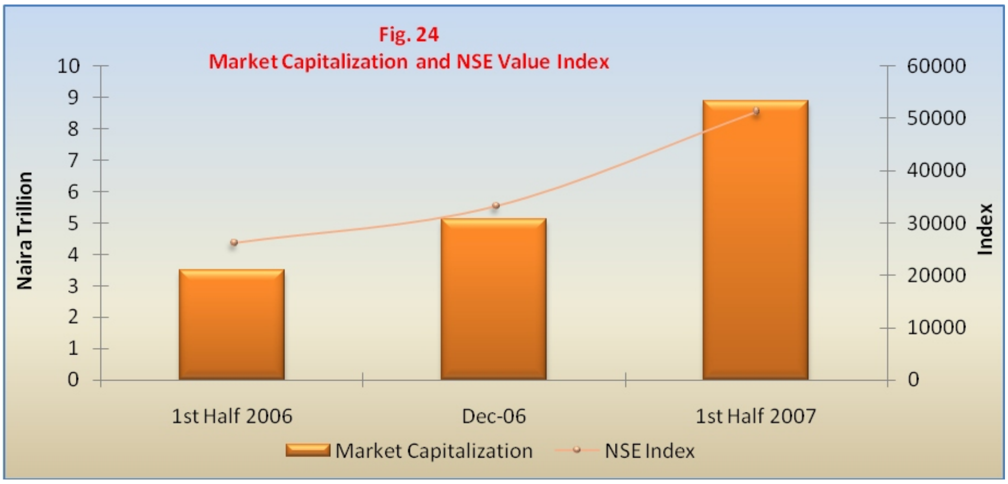
The new issues market remained active during the first half of the year with the approval of thirteen (13) fresh offers, four (4) public offers, six (6) right issues, three (3) private placements, six (6) supplementary offers and one debt to equity conversion. The volume and value of these issues amounted to 26.78 billion shares and N310.78 billion, respectively.

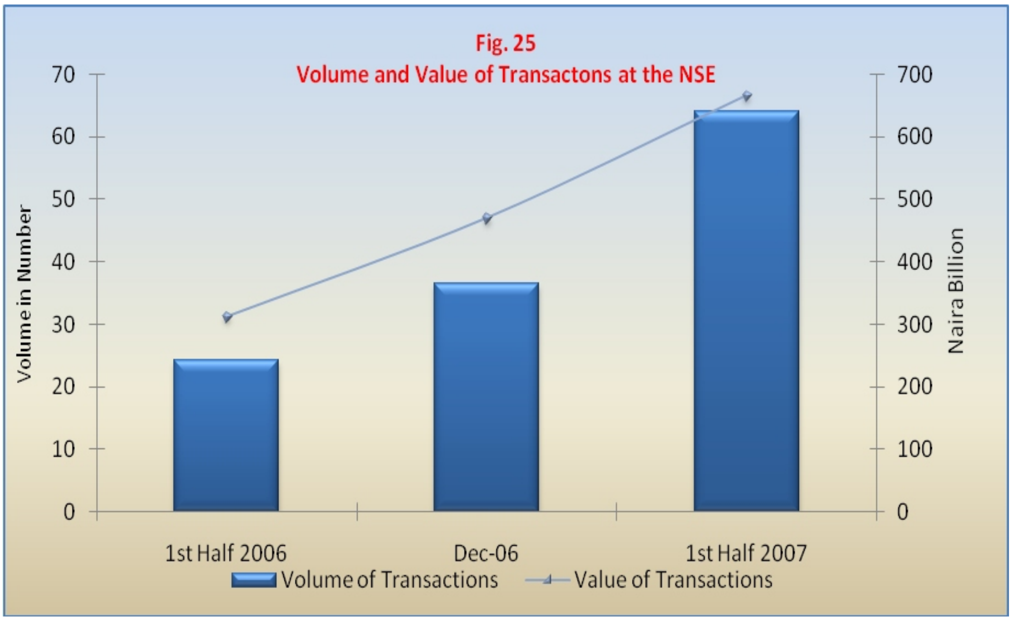
The first of the six series of the fourth FGN bonds, valued at N270.0 billion, were auctioned by the Debt Management Office (DMO). The six series of the bond were substantially oversubscribed, reflecting public confidence in the securities. Overall, the 4th FGN Bond and the special FGN bond for the first half of 2007 stood at N281.7 billion, while subscription and allotment were N622.90 billion and N281.7 billion, respectively. Thus, the total new issues in the first six months of the year stood at N281.7 billion.

### 3.1.5.3 The Secondary Market

The total market turnover of the secondary segment of the market rose by 163.8 per cent to 64.1 billion shares valued at N666.2 billion, compared with 24.3 billion shares valued at N312.7 billion in the corresponding period of 2006. The development was attributable to the increased public awareness of the high returns on investments in the market.

A sectoral analysis of developments in the market showed that the banking sub-sector remained the most active on the Exchange, with a transaction volume of 52.5 billion shares valued at N407.4 billion, representing 81.9 per cent of the total stocks traded. The insurance sub-sector came second following the conclusion of the recapitalisation exercise in the sub-sector.



### 3.1.5.4 Value Index of Equities

The all-share index of the Nigerian Stock Exchange rose by 96.2 per cent to 51,330.46 (1984=100) at end-June 2007, compared with 26,161.15 (1984=100) recorded at end-June 2006. The high transactions from blue chip stocks boosted the all share index. The index also rose by 54.7 per cent when compared the level at end December 2006.

### 3.1.6 Monetary Outlook for the Rest of 2007

The growth of the major monetary aggregates which was modest in the first half of 2007 is projected to rise in the second half of the year. This expectation is anchored on the seasonal increase in economic activities in the third quarter of the year which would likely spur the growth of both M2 and reserve money above the targets for the fiscal year. Consequently, excess liquidity will likely persist and remain a major challenge of monetary management for the rest of the year. This will therefore, require proactive aggressive liquidity mop-up actions by the CBN in order to meet the end-year targets.

**Box 3: Recent Developments in the Nigerian Capital Market**

In an effort to strengthen and reposition the operators in the Nigerian Capital Market in order to cope with the expected challenges and global competition, the Federal Government approved a new minimum capital base for all capital market operators in the country during the period under review. Specifically, the policy was aimed at ensuring that only well capitalized and properly structured organizations operate in the capital market. Under the new capital base, the minimum paid-up capital for issuing houses was increased from N150 million to N2.0 billion; brokers/dealers, from N70.0 million to N1.0 billion; clearing and settlement agency, from N500.0 million to N1.0 billion; and Registrars, from N50.0 million to N500.0 million. Underwriters were required to raise their minimum capital base from N100 million to N2.0 billion; fund/portfolio managers, from N20.0 million to N500.0 million, while corporate sub-brokers which had capital base of N5.0 million were to raise it to N50.0 million.

Operators not affected by the upward review included stock/commodities exchanges, capital trade points, commodities brokers, venture capital managers and individual investment advisers. Others are consultants (individual and corporate), rating agencies, corporate investment advisers and trustees. This was aimed at encouraging a smooth take off of these relatively new areas of capital market operations in Nigeria. Existing operators were given up to December 31, 2008 by the Securities and Exchange Commission (SEC) to comply with the new capital requirements either through capital increases or mergers/acquisitions, as no extension would be granted.

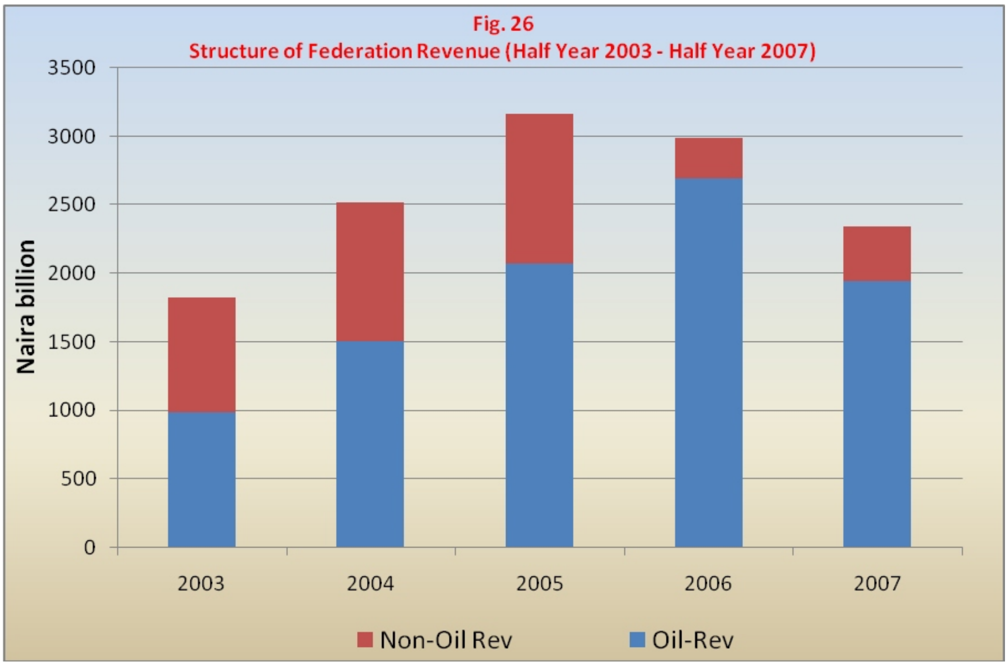
A 40 per cent reduction in all capital market fees for both primary and secondary market transactions was approved during the period under review. The reduction in cost was the culmination of industry-wide efforts at ensuring that the domestic capital market was made more competitive to attract both local and foreign investments into the country. Consequently, average equities transaction cost in the primary market was reduced from 6.92 to 4.32 per cent, while transaction cost on bonds dropped from 7.03 to 4.79 per cent. For the secondary market, equities transaction cost on the buy side was reduced from 4.07 to 2.36 per cent, while the sell side is now 2.65 per cent down, from 4.12. The new fee regime came into effect on April 24, 2007.

Other approvals during the period included 80 per cent mandatory underwriting for public offers; and a code of conduct for shareholders' associations in Nigeria. This was to reduce the incidence of under-subscription and ensure that the issuing houses and stockbrokers have higher stakes in the issues they bring to the market.

## 3.2 FISCAL OPERATIONS

### 3.2.1 FEDERATION ACCOUNT OPERATIONS

Total federally-collected revenue which stood at N2,344.9 billion during the first half of 2007 was 4.9 and 21.6 per cent lower than the proportional budget estimate and the actual revenue in the corresponding period of 2006, respectively. The decline in revenue relative to the budget estimates was largely due to the restiveness in the Niger Delta region which hampered crude oil production. This was however slightly moderated by the improved receipts from non-oil sources. Further analysis indicated that oil-revenue accounted for 83.0 per cent, while non-oil revenue accounted for the balance. At N1,945.4 billion, gross oil-revenue fell by 27.8 per cent below the level in the corresponding period of 2006, while non-oil revenue rose by 35.2 per cent to N399.4 billion over the same period, owing to the appreciable increase in the receipts from custom and excise duties.




Of the federally-collected revenue, the sum of N1,587.7 billion or 67.7 per cent was transferred to the Federation Account, while the balance went to Joint Venture Cash Call (11.8 per cent), Excess Crude Oil/PPT/Royalty Account (19.9 per cent) and "Others" (0.6 per cent).

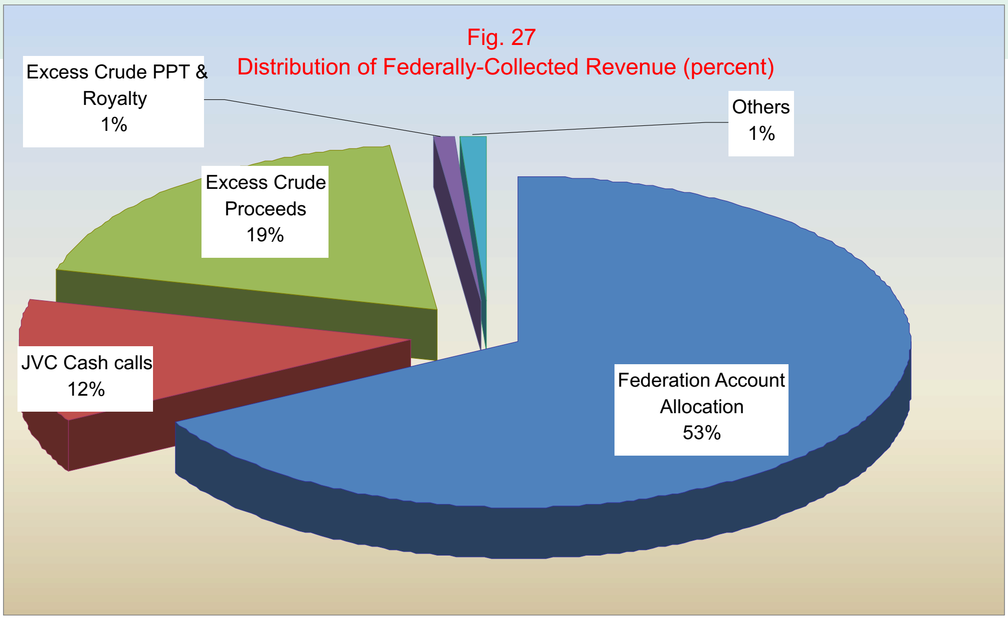



Fig. 27
Distribution of Federally-Collected Revenue (percent)

### 3.2.2 Federal Government Finances

#### 3.2.2.1 Federal Government Retained Revenue

At N1,143.6 billion, the Federal Government retained revenue was 19.9 and 47.1 per cent higher than the proportional budget estimate and the level in the corresponding period of 2006, respectively. This was as a result of the receipts of N100.00 billion from the FGN Natural Resources Development Account, issuance of the 4th FGN Bonds and the sharing of N183.4 billion from the excess crude account during the period. Analysis of the retained revenue revealed that the share from Federation Account was N672.7 billion, VAT Pool Account N19.9 billion, Federal Government Independent Revenue N22.1 billion, TBs/Bond Issues N130.9 billion, share of excess crude account N183.4 billion, with "others" accounted for the balance.

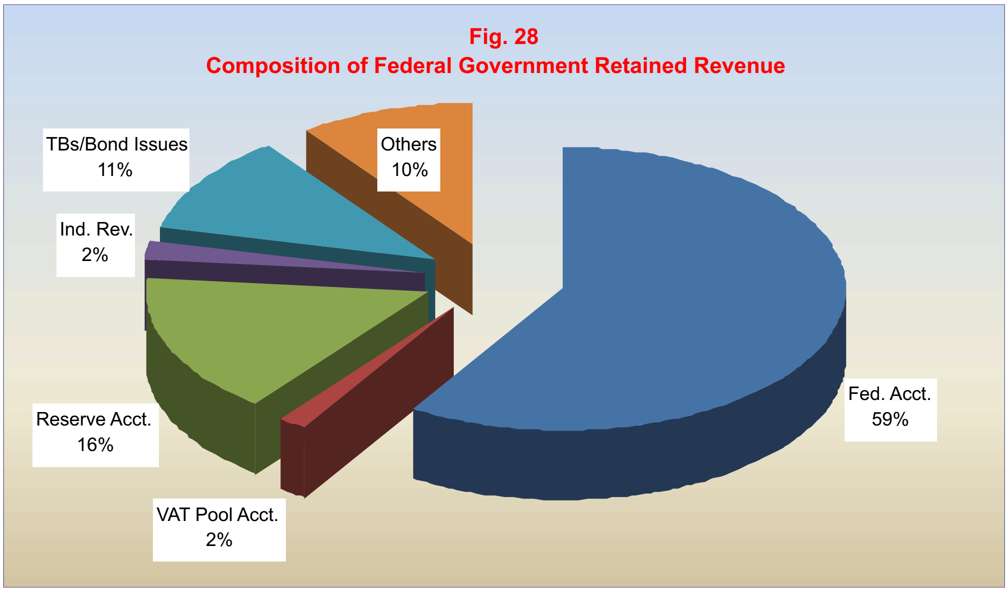
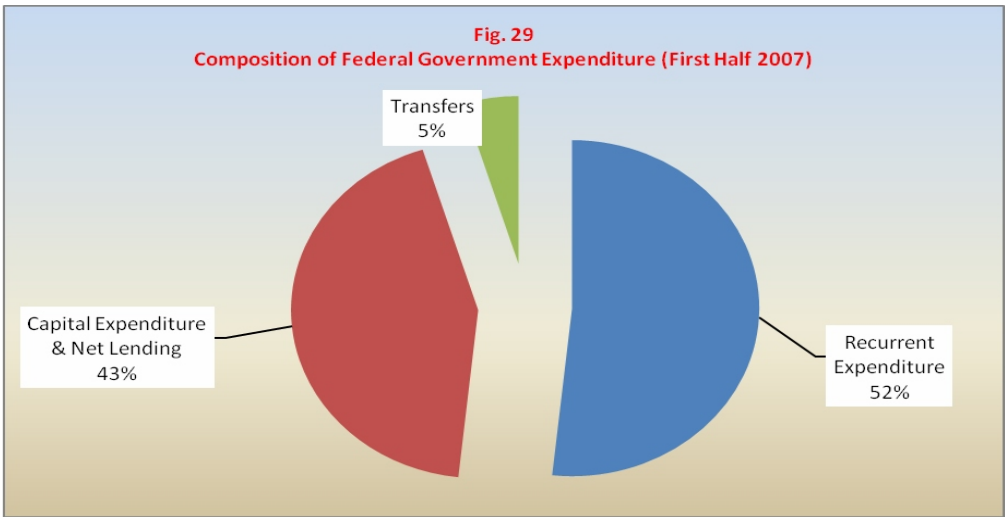


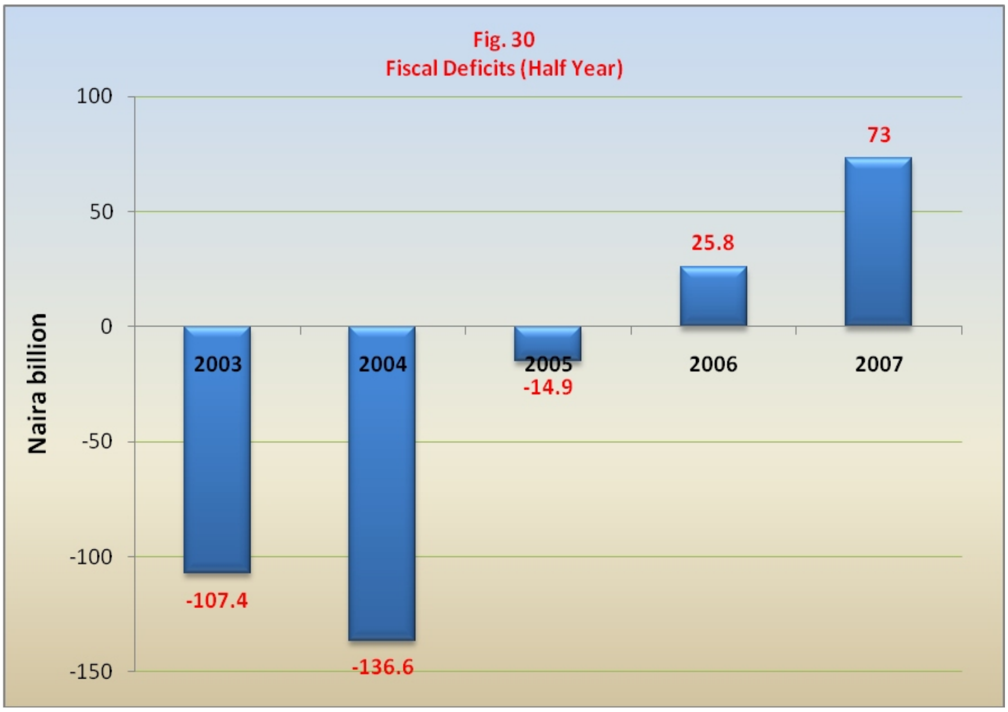

**Fig. 28**
**Composition of Federal Government Retained Revenue**

### 3.2.2.2 Total Expenditure of the Federal Government

Aggregate expenditure of the Federal Government stood at N1,070.6 billion. This was 12.5 per cent lower than the proportional budget estimate, but 42.4 per cent higher than the expediturel in the corresponding period of 2006. The lower total expenditure relative to the budget estimate resulted from a decline in interest payments on domestic debt. A breakdown of total expenditure showed that recurrent and capital expenditure accounted for 51.7 and 43.5 per cent of the total, respectively, while transfers accounted for the balance of 4.8 per cent.

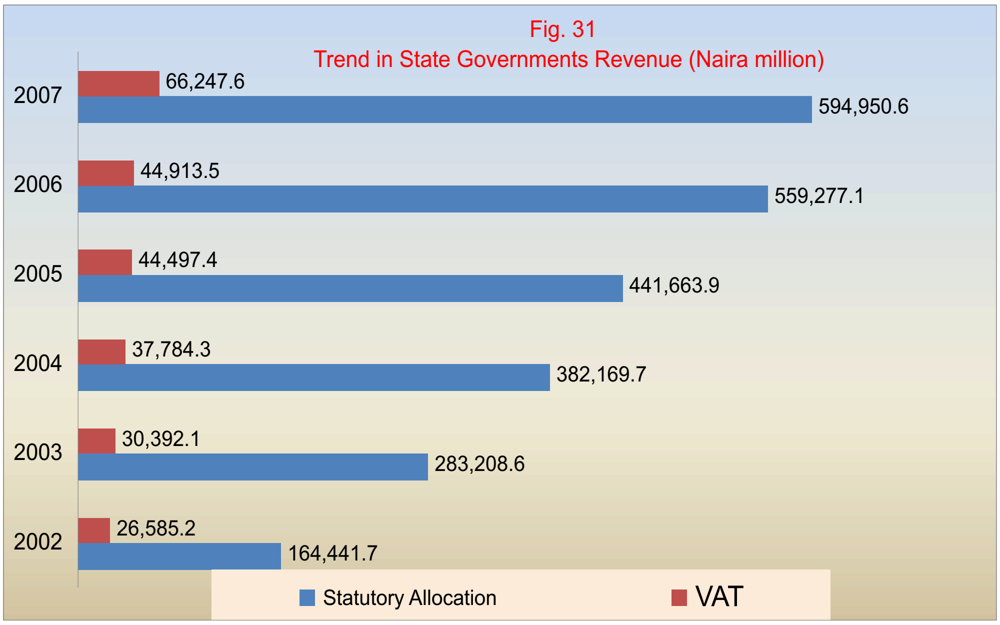



Thus, the fiscal operations of the Federal Government resulted in an overall surplus of N73.0 billion as against the proportional budget deficit estimate of N269.8 billion.



### 3.2.3 STATE GOVERNMENT FINANCES

Total revenue of the State Governments from the Federation Account (including excess crude) and VAT Pool Accounts amounted to N661.20 billion in the first half of 2007. This inducted an increase of 9.4 per cent over the receipts in the corresponding period of 2006. Analysis of the revenue showed that allocations from the Federation Account (including 13 per cent derivation fund and excess crude) amounted to N594.95 billion, while revenue from the VAT Pool Account was N66.25 billion. The receipts from the Federation and VAT Pool Accounts rose by 6.4 and 47.5 per cent, respectively, over the levels in the corresponding period of 2006.




### 3.2.4 LOCAL GOVERNMENT FINANCES

Statutory allocation to the 774 Local Governments from the Federation Account (including excess crude) and VAT Pool Accounts was N323.8 billion up by 2.4 per cent from the total receipts in the corresponding period of 2006. The improved revenue was due to a significant increase in the allocation from the VAT Pool Account. A breakdown of the receipts showed that the share of the Federation Account was N274.14 billion or 84.7 per cent as against the 91.7 per cent in the corresponding period of 2006, while that of VAT Pool Account was N49.69 billion or 15.3 per cent as against 14.0 per cent in the preceding year. Analysis of the allocation on state basis indicated that Kano, Lagos and Katsina topped with 5.7, 5.1 and 4.1 per cent of total, respectively, while Gombe, Bayelsa and Abuja ranked least with 1.5, 1.2 and 1.0 per cent, respectively.

Fig. 32
Statutory Allocation to Local Governments (First Half 2007)

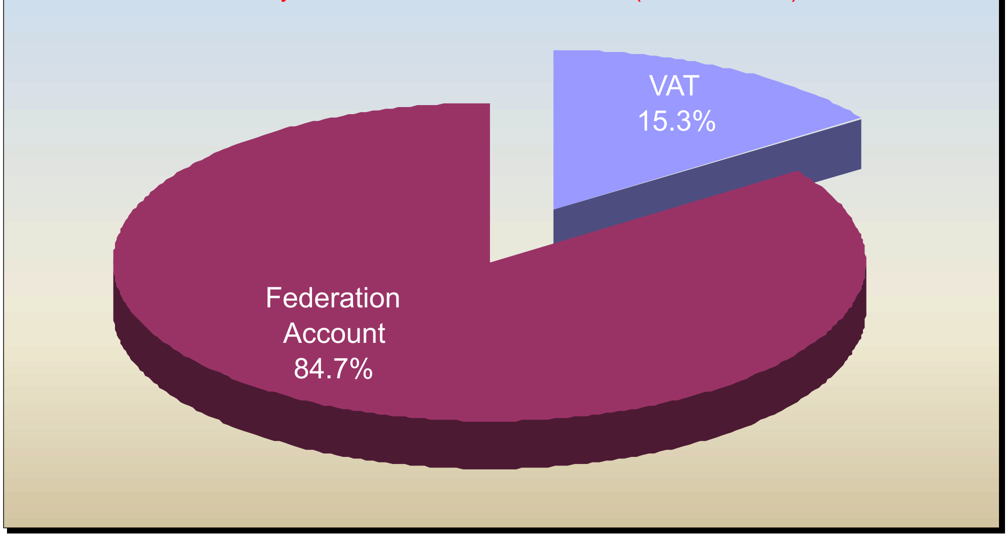
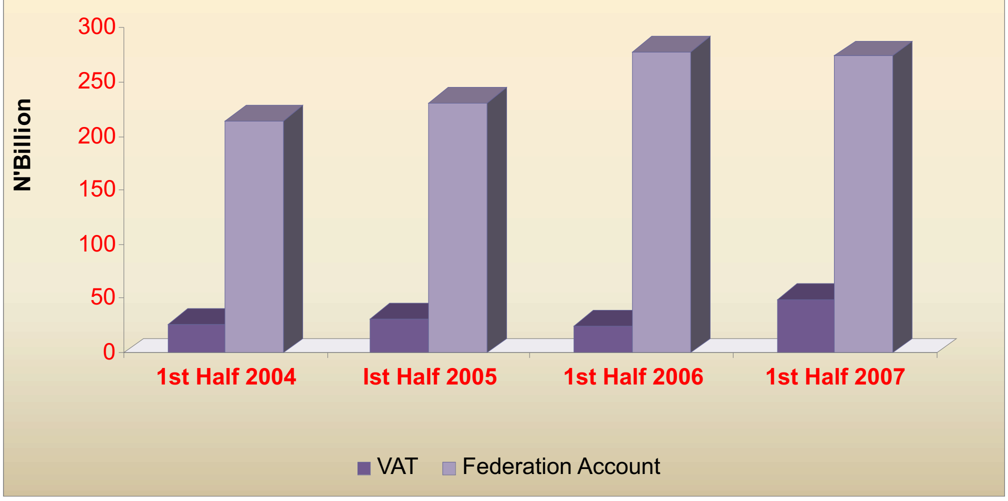



Fig. 33
Local Government Statutory Allocation, 2004-2007




### 3.2.5 PUBLIC DEBT

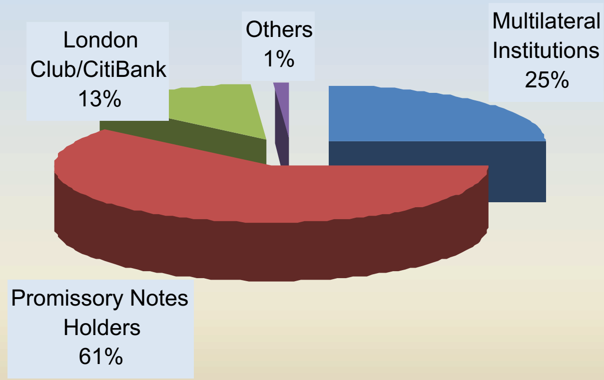
#### 3.2.5.1 Domestic Debt

The estimated Federal Government's securitized domestic debt outstanding increased by 30.5 per cent over the level at end-June 2006 to N2,056.9 billion. The increase was due to the issuance of the 4th FGN Bonds worth N281.7 billion in tranches beginning from January 2007 which was over-subscribed to the tune of N329.6 billion by the end of the first-half of the year. The banking system with an estimated 75.5 per cent remained the dominant holder of the total debt, while the balance of 24.5 per cent was held by the non-bank public. Domestic debt service payments estimated at N81.63 billion, was 38.4 and 1.6 per cent lower than the proportional budget estimate and the level in the corresponding period of 2006.

### 3.2.5.2 External Debt

Provisional data from the Debt Management Office indicated that the Federal Government's stock of external debt at end-June 2007 was US$3.49 billion. Multilateral Institutions accounted for US$2.82 billion or 84.2 per cent, while the balance of US$0.53 billion or 15.8 per cent was owed to the "Others" category of creditors. The total external debt service payments amounted to US$0.78 billion. A breakdown of external debt service payments showed that Promissory Notes accounted for 61.0 per cent, Multilateral Institutions 24.8 per cent, London Club 13.1 per cent, while "Others" accounted for the balance of 1.1 per cent.

Fig. 34
Breakdown of External Debt Service Payments to Creditors




### 3.2.6 FISCAL OUTLOOK

The fiscal operations of the Federal Government is expected to result in an estimated moderate surplus of about 0.5 per cent of the GDP by the end of the fiscal year in view of the expected sustained rise in the average crude oil prices. The sustained industrial growth in China and India are expected to exert pressure on the demand for crude oil and consequently pent-up the prices in the international oil market, while the protracted crisis in Iraq, the restiveness in the Niger Delta and the recent hurricane "Dean" in the Gulf of Mexico would likely constrain world oil output.

Furthermore, the continued sharing of the excess crude reserve to the three tiers of government may exacerbate fiscal profligacy, particularly at the sub-national levels and exert pressure on monetary aggregates, if such outlays are not on capital projects with positive linkages with the rest of the economy. Expenditure associated with the actualization of the Federal Government's desire to address infrastructural decay, particularly the power sector, may spur fiscal expansion that could seriously challenge liquidity management by the monetary authority. In addition, the Federal Government's decision to meet the 15.0 per cent wage increase from capital vote is likely to exert pressure on domestic prices.

## 3.3 REAL SECTOR DEVELOPMENTS

Provisional data from the National Bureau of Statistics (NBS) indicated that the Gross Domestic Product (GDP) at 1990 constant basic prices grew by 5.69 per cent in the first half of 2007 compared with 5.3 per cent recorded in the corresponding period of 2006. The aggregate growth was largely driven by the non-oil sector which rose by 9.2 per cent and contributed 76.8 per cent to the GDP while the oil sector output declined by 5.87 per cent and contributed the remaining 33.2 per cent of GDP. The main drivers of growth in the non-oil sector were Services (15.1%), Agriculture (6.80%) and Industry (6.60%). Sectoral contributions to GDP were

Agriculture (39.89%), Services (34.56%) and Industry (25.55%). The increase in industrial production was driven by the manufacturing sub-sector as mining output and electricity consumption declined.

Inflationary pressure moderated as the year-on-year inflation rate fluctuated between 8.5 per cent as at end-December, 2006 to 6.4 per cent in June 2007. The twelve-month moving average rate also declined from 15.5 per cent in June 2006 to 5.9 per cent in June 2007.

### 3.3.1 Agriculture

#### 3.3.1.1 Agricultural Policies and Institutional Support

The major policies introduced in 2006 were sustained in the first half of 2007. In line with the policy on fertilizer procurement, the Federal Government approved the procurement of 528,000 metric tonnes of fertilizer worth N33.0 billion for the use of farmers in the 2007 cropping season. It also initiated a public-private partnership for cotton production in 24 cotton producing states of the federation by setting aside N20.0 billion for the procurement of chemicals for farmers. The period of accessing the N50.0 billion agricultural loan scheme was extended to the end of the year, while the distribution of the N550.0 million Millennium Development Goals (MDGs) loans to farmers was flagged-off during the period.

#### 3.3.1.2 Agricultural Production and Prices

At 194.8 (1990=100), the provisional aggregate index of agricultural production rose by 7.4 per cent, compared with 6.2 per cent in the first half of 2006. The observed growth was broad based. The output of staples increased by 10.7 per cent, compared with 9.8 per cent in the first half of the preceding year, while that of 'other crops' rose by 6.2 per cent, compared with 8.1 per cent in 2006. The output of the livestock, fishery and forestry sub-sectors rose by 4.0, 9.3 and 1.1 per cent, respectively.

Growth in the agricultural sector was driven by the positive impacts of the earlier intervention measures of government, especially the presidential initiatives on various agricultural products, the National Fadama Project (NFP) and the National Special Programme for Food Security (SPFS). Other contributory measures were the zero tariffs on imported agro-chemicals, as well as stricter enforcement of the ban on importation of some agricultural products, such as poultry products and rice. These were complemented by good weather conditions. However, inadequate and untimely supply of farm inputs, especially fertilizers, persisted.

The domestic retail price of most food items declined, compared with the levels in the first half of 2006. The decline in the prices of ten of the fourteen commodities monitored ranged from 3.4 per cent for groundnut to 90.7 per cent for yellow maize. The development was attributable to increased production of the commodities, as farmers responded positively to the various government initiatives and the good weather conditions. However, the price of some commodities, such as yam flour, vegetable oil, palm oil and eggs increased by 4.8, 8.6, 26.6 and 33.5 per cent, respectively. Despite the resurgence of the avian influenza (bird flu) in the poultry sub-sector, poultry production and consumption were unaffected as measures were taken to curtail the spread of the disease.

The prices of Nigeria's major agricultural export commodities, at the London Commodities Market, increased in the first half of 2007. At 259.1 (1990=100), the dollar-based all commodities price index rose by 36.1 per cent over the level in the first half of 2006. Further analysis showed that of the six commodities monitored, the price indices of four; cotton, copra, soya bean and palm oil, rose by 0.7, 26.8, 48.6 and 51.2 per cent, respectively, while the price indices of coffee and cocoa declined by 5.5 and 49.2 per cent, respectively. The increase in the price of most commodities was attributed mainly to increased demand and supply shortages in the international market.

In Naira terms, the all commodity price index at 3,183.7 (1990=100), rose by 36.3 per cent, relative to the level in the first half of 2006. Further analysis showed that all the commodities monitored recorded price increases ranging from 0.8 per cent for cotton to 50.6 per cent for palm oil.

### 3.3.2 Industry

#### 3.3.2.1 Industrial Policy and Institutional Support

The Industrial Policy, as contained in the 2007 Federal Government budget, was anchored on the NEEDS. The overall objective was to achieve the following targets:

- annual growth of the manufacturing sector by at least 7.0 per cent;
- manufacturing capacity utilization of 70.0 per cent ;
- private sector contribution to total investment in industries of 70.0 per cent ;
- promotion of the private sector as the pivot in the industrialization process, through public-private partnership; and
- support for the development of the small and medium enterprises sub-sector

In the effort to achieve the aforementioned objectives, the government continued to pursue the policy of privatization of the state owned enterprises (SOEs) with the sale of the Port-Harcourt and Kaduna refineries in the first half of 2007. The Bureau of Public Enterprises (BPE) also received bids from three international companies to manage electricity transmission across the country. The Transmission Company of Nigeria was set up after the dissolution of the National Electric Power Authority (NEPA). In the meantime, the distribution of pre-paid meters to electricity consumers in the country continued with the aim of ensuring efficient distribution, timely payment for electricity as well a full recovery of revenues from power supply.

#### 3.3.2.2 Industrial Production

Activities in the industrial sector increased during the first half of 2007, as the index of industrial production at 124.8 (1990=100) rose by 0.2 per cent above the level attained during the corresponding period of 2006. The performance was reflected in the increase in manufacturing output as mining production and electricity consumption declined.

#### 3.3.2.3 Manufacturing

At 94.6 (1990=100), the estimated index of manufacturing production rose by 2.6 per cent relative to the corresponding period of 2006. The development was attributed largely to the increased surveillance activities by regulatory agencies such as National Agency for Food, Drug Administration and Control (NAFDAC) and the Standards Organisation of Nigeria (SON), import prohibition of some manufactured products as well as increased access to bank credit following the banking sector consolidation.

This development was corroborated by an impressionistic survey carried out on some manufacturing firms across the country by the CBN. The survey revealed that the capacity utilisation as at end-June 2007 was 46.1 per cent indicating an increase of 1.0 percentage point, compared with the corresponding period of 2006. However, energy inadequacy remained the most binding constraint to the efficient performance of the manufacturing sector as indicated by 54.3 per cent of the respondents. Other constraints by the respondents included delays of imported raw materials at seaports and influx of cheap products, which competed unfairly with locally produced goods.